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WEAKNESS ON THE GOODS PRODUCING SIDE HOLDS BACK GROWTH

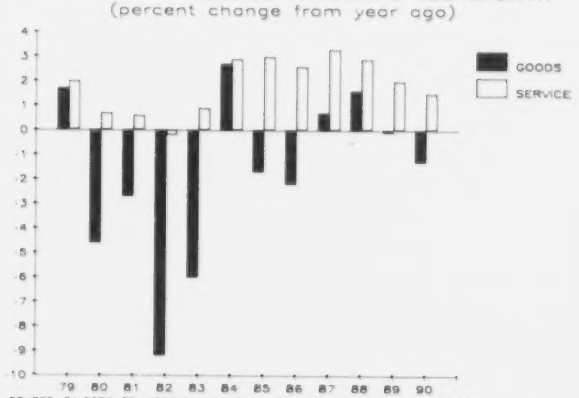
Trends through April suggest that a sluggish showing on the part of Pennsylvania's goods producers continues to hold down the overall rate of economic growth. Several measures of goods producing activity, including job trends, production activity, and building trends, point to some slack in these all-important industries. A major concern is that this weakness will spread into the service producing sectors. Indeed, April job trends point to some weakening in the fortunes of Pennsylvania's service producing industries.

Softness on the goods producing side in April accounts for much of the downtrend in the indices of coincidental and leading economic indicators. A pronounced drop in the real weekly earnings of manufacturing production workers helped push down the coincidental series. **One of the largest declines in the seasonally adjusted average factory workweek on record (dating back to 1972), leaving this measure of the factory sector's health at its lowest reading in nearly five years, contributed greatly to a large decline in the index of leading indicators in April. The index has now declined for three consecutive months and in six of the last seven (chart). Still, the general downtrend evident of late is not as pronounced as those prior to the onset of previous recessions. Hence, a severe slump does not appear to be likely in the foreseeable future.**

Simply put, the economic recovery in place since roughly 1983 is not reflected in job trends as they relate to Pennsylvania's goods producers. Over the 1983-1989 period, job levels in these industries declined in four years, including 1989 (chart). That sluggish performance has continued into the first four months of 1990 as jobs are off 1.3 percent from a year ago. Measures of the manufacturing sector's health have deteriorated considerably. April brings with it the third consecutive monthly drop in the number of factory jobs, seasonally adjusted. Production activity, as measured by the Pennsylvania Manufacturing Activity Index, remains on a downtrend. As mentioned above, both real earnings and hours worked also point down.

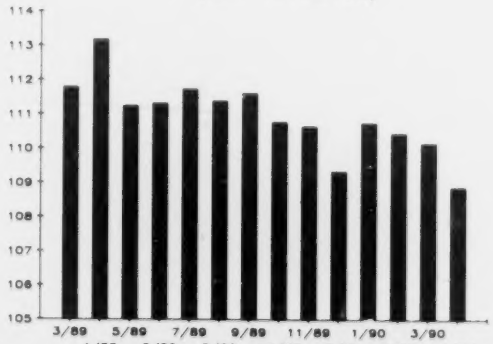
Elsewhere, **construction remains in the doldrums.** While the value of contract awards are up from March readings, totals are off considerably from a year ago. The number of new housing units authorized in April are down nearly 30 percent from a year ago, bringing the year-to-date decline to 16 percent. Declines are also evident on the nonresidential side. March and April typically bring the first signs of

PA GOODS AND SERVICE PRODUCING JOB GROWTH
(percent change from year ago)



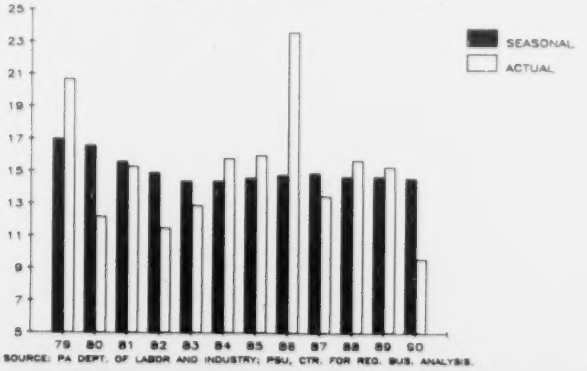
SOURCE: PA DEPT. OF LABOR AND INDUSTRY; PSU, CTR. FOR REG. BUS. ANALYSIS.

PENNSYLVANIA COMPOSITE INDEX
OF LEADING INDICATORS
(Jan. 1972=100)



SOURCE: PSU, CENTER FOR REGIONAL BUSINESS ANALYSIS.

PA APRIL CONSTRUCTION JOBS:
EXPECTED SEASONAL AND ACTUAL TRENDS
(absolute change from March)



SOURCE: PA DEPT. OF LABOR AND INDUSTRY; PSU, CTR. FOR REG. BUS. ANALYSIS.

improvement in building activity, with the result usually being some rather pronounced job gains. Based upon historical trends, about 15,000 additional construction jobs are expected in April simply due to seasonal improvement (chart). Over the 1984-1989 period, April job gains were larger than expected in five of the six years, evidence of strength in these industries throughout much of the period. This April, however, job trends do not measure up to expectations as only 9,000 new positions are added to payrolls. The end result is a seasonally adjusted decline in job totals.

It is doubtful that April trends are a sign of things to come. **While future months are not likely to result in significant improvement in Pennsylvania's goods producing industries, deterioration on the order of that recorded in April is not expected to continue.** It may well be that the timing of the Easter holiday accounts for some of the apparently sharp dropoff in activity.

New Pennsylvania building permit authorizations (percent change from year ago)

	Apr.	Pct. chg.	Year-to-date	Pct. chg.
Residential	3,668	– 28.9	12,399	– 15.9
Nonresidential	2,200	– 16.6	5,493	– 7.6

Source: U.S. Dept. of Commerce, Bureau of the Census.

While still positive, service producing job growth continues to ease. After registering 3.3 percent in 1987, growth declined in both 1988 and 1989. The 1.5 percent year-to-date gain through April of this year is the smallest since 1983. In April, job levels are down on a seasonally adjusted basis from March. Still, they remain just below record high

Economic Activity in Pennsylvania	UNADJUSTED DATA			SEASONALLY ADJUSTED DATA			SEASONALLY ADJUSTED INDEXES (1977 = 100)		
	1990		1989	1990		1989	1990		1989
	March	*April*	*April*	*March*	*April*	*April*	*March*	*April*	*April*
Pennsylvania Industries									
All nonagricultural industries									
No. of wage and salary jobs (thous.)[1]	5,108*	5,137	5,113	5,148	5,137	5,112	112.8	112.5	112.0
Service Producing									
No. of wage and salary jobs (thous.)	3,834	3,854	3,806	3,848	3,845	3,797	128.6	128.5	126.9
Transportation and public utilities	253	253	257	254	252	256	97.0*	96.4	97.8
Wholesale trade	282	282	279	283	282	280	127.8*	127.1	126.1
Retail trade	884*	890	888	900	897	896	125.5	125.1	124.9
Finance, insurance & real estate	296	296	295	298	297	296	137.2*	136.5	135.9
Service & miscellaneous	1,399	1,409	1,378	1,406	1,405	1,373	163.0	162.9	159.2
Federal government	143*	147	143	144	146	142	112.2*	113.7	110.9
State & local government	577	578	564	566	566	551	97.1	97.1	94.6
Goods Producing									
No. of wage and salary jobs (thous.)	1,273	1,282	1,306	1,300	1,291	1,315	82.6	82.1	83.6
Construction	217	226	227	238	233	234	129.6*	126.9	127.3
Mining	27	27	27	28	28	28	57.7	57.3	57.3
Manufacturing	1,029	1,028	1,051	1,034	1,031	1,054	77.1	76.8	78.6
Durable goods	583	584	604	587	585	604	72.5	72.2	74.6
Nondurable goods	446	444	448	447	446	450	84.1	83.9	84.6
Ave. wkly. hrs. worked by prod. workers	40.5*	39.4	40.9	40.7*	39.6	41.1	103.0	100.2	104.0
Total wkly. person-hours worked (mils.)	28.8	28.0	29.8	29.0	28.2	30.0	75.6	73.4	78.2
Total wkly. payroll (mil. dols.)	314.7*	306.0	315.0	317.5*	308.2	317.4	141.3	137.2	141.3
Average hourly earnings (dollars)	10.94	10.93	10.58	10.97	10.92	10.57	187.6	186.7	180.7
Average weekly earnings (dollars)	443.07	430.64	432.72	445.30	433.24	435.51	192.5*	187.3	188.3
Steel production (thous. tons)	954	1,026	1,120	n.a.	n.a.	n.a.	40.4	40.7	44.3
Industrial electric power sales (mil. kwh)	3,797	3,713	3,750	3,779	3,763	3,816	102.3	101.9	103.3
Mining									
Anthracite coal (thous. net tons)	334	297	270	380	320	301	77.7	65.5	61.5
Bituminous coal (thous. net tons)	6,426	5,821	5,900	5,841	5,682	5,965	82.8	80.6	84.6
Construction contracts awarded (mil. dols.)									
Total	796.6	816.5	1,027.7*	675.0	796.9	1,034.0*	209.8	247.7	321.4*
Residential building	337.9	337.3	460.7*	297.5	298.7	411.1*	211.4	212.2	292.1*
Nonresidential building	299.8	280.5	409.2*	258.3	315.5	483.5*	238.1	290.8	445.7*
Nonbuilding (utilities and public works)	158.8	198.7	157.8*	119.2	182.7	139.4*	164.5	252.1	192.3*
Employment of Pennsylvania Residents									
Employed, no. of persons (thous.)	5,599	5,562	5,578	5,695	5,602	5,621	118.5	116.6	117.0
Unemployed									
No. of persons (thous.)	316	315	235	307	340	260	76.6	84.8	64.7
Rate (percentage of labor force)	5.3	5.4	4.0						
Rate, seasonally adjusted				5.2	5.7	4.4			
Civilian labor force, no. of persons (thous.)	5,915	5,878	5,813	6,002	5,942	5,881	115.3	114.1	112.9
Initial claims for unemployment benefits	88,117	88,941	69,290	103,381	92,942	77,486	72.2	64.9	54.1

Consumer Prices, all items	Urban Indexes (1982-84 = 100) 1990 *March*	*April*	1989 *April*	Percentage Change *Month Ago*	*Year Ago*
U.S. city average	128.7	128.9	123.1	0.2	4.7
Philadelphia	133.6	134.3	126.7	0.5	6.0
Pittsburgh	n.a.	124.9	119.2	n.a.	4.8

[1] Total includes workers on strike. * = figure revised § = figure for March 1989 n.a. = data not available
SOURCES AND DEFINITIONS OF DATA ARE AVAILABLE ON REQUEST.

Pennsylvania retail sales
(millions of dollars; pct. chg. from year ago)

	March	Pct. chg.	Year-to-date	Pct. chg.
Total	6,964	3.9	19,019	4.4
Durables	2,462	1.9	6,721	4.1
Bldg. mat.	251	-2.3	667	1.1
Auto dlrs.	1,483	-4.0	3,933	0.4
Furniture	331	18.6	952	14.6
Other	397	18.5	1,169	11.4
Nondurables	4,502	5.0	12,298	4.5
Gen. mdse.	703	5.4	1,696	4.7
Food/grocery	1,478	7.8	4,122	5.0
Gas	399	7.0	1,146	7.5
Apparel	344	5.8	885	5.6
Eat/drink	801	3.5	2,210	3.7
Drugs	254	-9.0	757	-1.4
Other	523	5.2	1,482	4.7

Seas. adj. total: March 7,056
February 6,917

Source: Tot./Dur./Nondur.-U.S. Dept. of Commerce, Bur. of the Census.
Seas. adj. total-PSU, Ctr. for Reg. Bus. Analysis.
Data in the sub-categories of the durable and nondurable groups are subject to relatively large sampling variability. As a result, only pct. changes are shown.

readings. **Retail sales continue to increase, but at a rather disappointing pace. During this year's first quarter, sales are up 4.4 percent from a year ago. While this does represent some improvement over 1989's 3 percent gain, it falls well short of the 6 percent gain nationwide and the 5 percent gain in the overall level of consumer prices.** Compared to last year, sales growth is up across the board on the durable goods side (chart). The performances of the several nondurable goods categories tracked are somewhat mixed relative to 1989 trends. In the largest category, food and groceries, sales growth is up slightly so far in 1990. In seven of the 11 groups examined, growth so far in 1990 is off from the average of the past decade. Through March, the number of new motor vehicles registered in Pennsylvania continues to trend down.

Retail trade jobs stand just barely above year-ago readings, albeit at the highest reading for April on record. **Even growth in the historically strong service industries appears to be easing a bit. Between 1982 and 1989, job gains in these**

New Pennsylvania motor vehicle registrations
(percent change from year ago)

	Total registrations	Pct. change
March	49,160	-4.0
1990 YTD	149,539	-2.7
12-month total	661,227	-7.3

Source: R.L. Polk & Co.

industries averaged 4 percent on an annual basis. So far this year, job growth comes in at a lower, but still respectable, 2.6 percent.

These general trends are reflected in a generally poor showing on the employment/unemployment front in April. Seasonally adjusted employment readings are off by 90,000 from March with the result being a jump in the jobless rate of 0.5 percentage point to 5.7 percent. Along with a similar reading in February, this represents the highest jobless rate in approximately three years. (Some improvement is apparent, however, in the employment and unemployment situation based upon May figures, the first indicator of the economy's health for the month.)

In a nutshell, the Pennsylvania economy appears to be moving sideways, as opposed to up or down. Given the lack of convincing evidence of any improvement in the nation's economy, conditions are unlikely to change in the near future.

Personal Income Report

Three trends are apparent from an examination of the most recent developments on the personal income front in Pennsylvania. Most importantly, the economic recovery which began in the early 1980s remains in place. Secondly, available evidence suggests that Pennsylvania continues to perform more on par with the U.S. after a decade of below-average growth. Finally, disparities across sectors and regions remain evident in Pennsylvania.

Personal income comes to $209.8 billion in Pennsylvania in 1989, up 7.8 percent from 1988 readings. This represents the strongest gain since 1981 and compares favorably with the 7.6 percent advance recorded nationwide. On a per capita basis, personal income comes to $17,422 in 1989, up 7.4 percent from a year ago. Nationally, per capita income totals $17,567 for a 6.5 percent gain. A good indicator of individual economic well-being is per capita personal income, adjusted for price changes. This measure of average "real" income has increased seven consecutive years in Pennsylvania (chart) with no signs yet of a considerable slowdown.

With respect to the Commonwealth's performance relative to the nation's, improvement over the past few years is evident. Over, roughly, the 1975-1986 period, Pennsylvania continuously trailed the growth rate in personal income nationwide, often by considerable margins (chart). Since then, however, the State has maintained personal income growth rates pretty much in line with national norms. Still, because of the Commonwealth's relatively poor showing in earlier years, ground has been lost. In 1989, Pennsylvania accounts for 4.8 percent of U.S. personal income. In 1975, the State accounted for 5.5 percent of the total. So, while economic improvement has been, and is, evident in Penn-

1989 personal income by major source: Pennsylvania and the United States (millions of dollars)

	Pennsylvania		U.S.
	1989	Pct. chg. from 1988	Pct. chg. from 1988
Earnings by place of work	146,065	6.6	6.4
By type			
Wage and salary disbursements	117,811	6.4	6.2
Other labor income	12,439	8.5	8.5
Proprietors' income	15,815	6.3	6.2
By industry			
Farm	1,060	15.1	5.5
Nonfarm	145,005	6.5	6.4
Private	126,458	6.4	6.2
Ag. serv., for., fish., and other	636	5.0	3.8
Mining	1,296	1.9	– 0.7
Construction	9,605	5.1	2.7
Manufacturing	33,569	3.0	3.9
Nondurable goods	13,025	4.3	4.6
Durable goods	20,545	2.2	3.6
Transportation and public utilities	9,610	5.7	5.4
Wholesale trade	9,318	8.4	7.6
Retail trade	13,788	6.8	5.7
Finance, insurance, and real estate	9,090	3.7	3.8
Services	39,546	10.3	10.2
Government	18,548	7.1	7.4
Federal, civilian	4,519	6.5	8.0
Federal, military	680	– 5.7	3.6
State and local	13,348	8.1	7.7
Total personal income	209,751	7.8	7.6
Nonfarm personal income	208,691	7.7	7.6
Net earnings[1]	135,674	6.3	6.2
Dividends, interest and rent	37,811	13.3	12.9
Transfer payments	36,266	7.8	8.1

SOURCE: U.S. Department of Commerce, Bureau of Economic Analysis, Regional Economic Information System, April 1989.

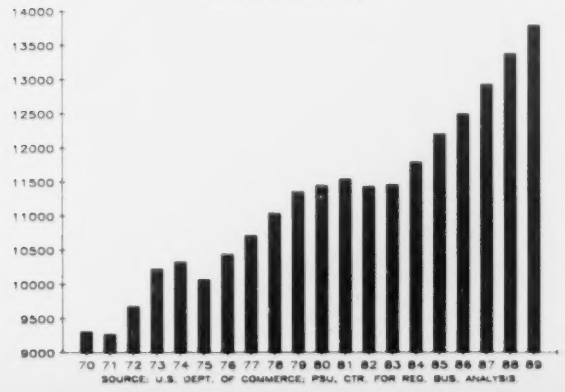
[1]Total earnings by place of work less personal contributions for social insurance plus an adjustment for residence.

sylvania, it can be argued that the State has lost a portion of its share of domestic economic activity.

In terms of sectoral performances, the services industries continue to lead the way as the earnings of workers employed in these establishments are up more than 10 percent from a year ago. Both the manufacturing and finance-related industries turned in relatively sluggish showings with respect to earnings growth in 1989.

Despite income- and employment-related trends which suggest that the goods producing sector's (and especially, manufacturing's) role in the Pennsylvania economy is diminish-

REAL PENNSYLVANIA PER CAPITA PERSONAL INCOME
(1982 dollars)



1988 total and per capita personal income: Pennsylvania metropolitan areas and counties

	Total personal income (millions of dollars)		Per capita personal income (dollars)	
	1988	Pct. chg. from 1987	1988	Pct. of PA ave. 1988
MSAs				
A'town-Beth MSA*	11,637	7.7	17,185	106.0
Carbon	760	6.7	13,537	83.5
Lehigh	5,077	6.8	17,589	108.4
Northampton	4,008	8.3	16,450	101.4
Altoona MSA (Blair)	1,686	5.0	12,724	78.5
Beaver MSA (Beaver)	2,501	4.1	13,172	81.2
Erie MSA (Erie)	3,934	7.1	14,201	87.6
H'burg-Leb-Carl MSA	9,284	8.0	15,706	96.8
Cumberland	3,265	8.6	16,720	103.1
Dauphin	3,846	7.6	15,976	98.5
Lebanon	1,641	8.1	14,359	88.5
Perry	532	7.9	13,033	80.4
Johnstown MSA	3,078	6.4	12,280	75.7
Cambria	2,099	6.3	12,335	76.1
Somerset	979	6.5	12,166	75.0
Lanc MSA (Lancaster)	6,881	7.8	16,616	102.4
Philadelphia MSA*	91,046	8.1	18,504	114.1
Bucks	10,524	8.2	19,360	119.4
Chester	7,792	9.6	21,259	131.1
Delaware	11,364	7.4	20,407	125.8
Montgomery	16,743	8.1	24,351	150.1
Philadelphia	23,962	6.9	14,549	89.7
Pittsburgh MSA	34,521	6.8	16,484	101.6
Allegheny	24,127	7.1	17,816	109.8
Fayette	1,823	5.7	11,974	73.8
Washington	3,006	6.4	14,378	88.6
Westmoreland	5,565	6.2	14,695	90.6
Reading MSA (Berks)	5,857	7.3	17,798	109.7
Scr-Wilkes-Barre MSA	10,635	7.5	14,437	89.0
Columbia	804	6.5	13,181	81.3
Lackawanna	3,281	7.3	14,759	91.0
Luzerne	4,740	7.3	14,299	88.2
Monroe	1,423	9.9	15,221	93.8
Wyoming	387	7.2	13,634	84.1
Sharon MSA (Mercer)	1,608	7.4	13,140	81.0
St Coll MSA (Centre)	1,613	8.3	13,945	86.0
W'port MSA (Lycoming)	1,674	8.1	14,154	87.3
York MSA	7,031	8.6	17,132	105.6
Adams	1,139	8.4	15,326	94.5
York	5,892	8.6	17,532	108.1
Non-MSA counties				
Armstrong	1,070	5.3	13,729	84.6
Bedford	546	4.4	11,375	70.1
Bradford	816	7.2	12,645	78.0
Butler	2,235	7.5	14,570	89.8
Cameron	80	8.1	12,576	77.5
Clarion	516	5.3	12,353	76.2
Clearfield	1,015	5.7	12,422	76.6
Clinton	450	7.7	11,838	73.0
Crawford	1,091	6.3	12,692	78.3
Elk	526	6.5	14,317	88.3
Forest	56	7.7	11,723	72.3
Franklin	1,704	7.2	14,168	87.4
Fulton	171	8.9	11,903	73.4
Greene	444	3.0	11,185	69.0
Huntingdon	476	7.2	11,039	68.1
Indiana	1,113	6.0	12,091	74.5
Jefferson	614	5.7	12,868	79.3
Juniata	272	6.3	13,395	82.6
Lawrence	1,280	7.2	12,691	78.2
McKean	610	4.3	13,198	81.4
Mifflin	553	6.3	11,834	73.0
Montour	280	6.5	16,975	104.7
Northumberland	1,260	6.4	12,811	79.0
Pike	440	13.7	16,430	101.3
Potter	206	5.6	11,412	70.4
Schuylkill	2,160	7.8	14,020	86.4
Snyder	560	7.7	15,392	94.9
Sullivan	77	6.9	12,063	74.4
Susquehanna	496	6.2	12,147	74.9
Tioga	463	6.4	11,494	70.9
Union	478	8.4	13,692	84.4
Venango	865	4.6	14,171	87.4
Warren	650	7.1	14,248	87.8
Wayne	555	8.6	13,711	84.5
Pennsylvania	194,659	7.4	16,219	100.0

Source: U.S. Department of Commerce, Bureau of Economic Analysis, Regional Economic Information System, April 1990.

* Includes New Jersey counties contained in the MSA.

ing, it is best not to discount the importance of these industries in the State's economy, especially in relative terms. In 1989, these industries account for nearly 31 percent of all earnings in the Commonwealth (chart). Two decades ago, they accounted for 45 percent. Still, Pennsylvania remains more dependent on these industries than does the U.S. as a whole. Construction, mining, and manufacturing earnings account for just 28 percent of all earnings nationwide. These industries continue as a vital force in the Pennsylvania economy and the State's business cycle is very much dependent on developments in the goods producing sector.

Personal income data through 1988 are available for each of Pennsylvania's 67 counties. Not surprisingly, the strongest gains come in the easternmost regions of the Commonwealth. Specifically, except for the Reading area, each metro region in the eastern half of the State is characterized by stronger personal income growth than in Pennsylvania as a whole. The York region's 8.6 percent gain is the strongest of the State's 15 metro areas. In the western half of the Commonwealth, only the State College metro area has an above-average growth rate over the 1987-1988 period. (Mercer County equaled Pennsylvania's 7.4 percent gain.) In fact, Centre County's 8.3 percent gain is the second strongest in metropolitan Pennsylvania, a finding consistent with previous positive reviews of the region's economy. Beaver and Blair Counties are home to the lowest income growth rates in metropolitan Pennsylvania, 4.1 and 5 percent, respectively.

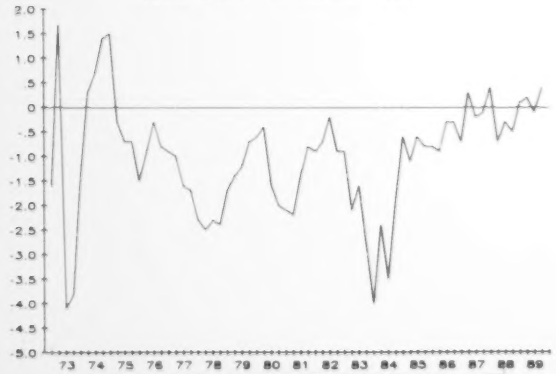
This east/west split is also apparent when trends in non-metro counties are taken into account. Furthermore, this split is not a recent development. Indeed, over the 1979-1988 period, all counties with above-average (above the State's 82.3 percent) personal income growth are found east of, and including, Centre County (chart). Especially strong growth is evident in the extreme northeast and southeast.

Generally similar conclusions are found as they relate to per capita income trends. The highest (relative to the State's $16,219) readings of per capita income are found in the southeast, with the lone notable exception being Allegheny County (chart). The Philadelphia metro region maintains a per capita reading which is 14 percent higher than the Statewide average and is home to the four highest county-level readings in the State.

As a group, those counties within Pennsylvania which are not included in a metro area come up short with respect to personal income trends and appear to be losing ground. These counties increased their share of personal income in the State throughout the 1970s, rising from 12 percent to over 13 percent of the total (chart). However, they have lost ground nonstop during the 1980s, so that as of 1988 they account for just 12.4 percent of the State's income.

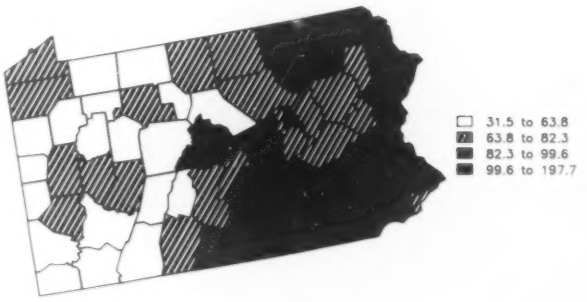
In sum, recent trends in Pennsylvania personal income should be interpreted rather favorably. They are perhaps the best indicator that the economic recovery remains on fairly solid ground. At the same time, some potential problems, many of which have been discussed in previous issues of the *Pennsylvania Business Survey*, are also evident in these trends. Most notably, differences are apparent across both sectors and geographic regions with respect to personal income trends.

PA AND U.S. PERS. INCOME GROWTH DIFFERENTIALS
(pct. pts.; PA minus U.S.)



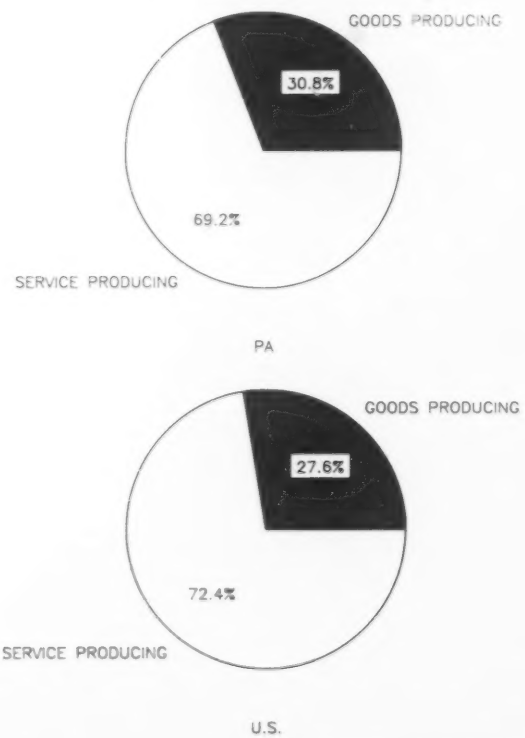
SOURCE: U.S. DEPT. OF COMMERCE; PSU, CTR. FOR REG. BUS. ANALYSIS.

1979-1988 COUNTY PERSONAL INCOME GROWTH
(percent)



SOURCE: U.S. DEPT. OF COMMERCE, PSU, CTR. FOR REG. BUS. ANALYSIS.

SHARE OF PA AND U.S. EARNINGS:
GOODS AND SERVICE PRODUCING INDUSTRIES

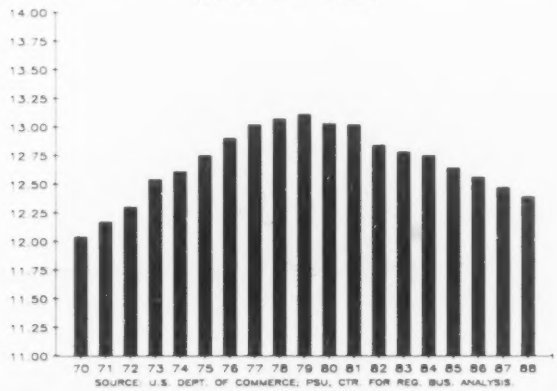


SOURCE: U.S. DEPT. OF COMMERCE, PSU, CTR. FOR REG. BUS. ANALYSIS.

1988 PA COUNTY PER CAPITA PERSONAL INCOME
(dollars)

SOURCE: U.S. DEPT. OF COMMERCE, BUR. OF ECON. ANALYSIS

NONMETROPOLITAN PA'S SHARE OF PERSONAL INCOME
(percent of total)



SOURCE: U.S. DEPT. OF COMMERCE; PSU, CTR. FOR REG. BUS. ANALYSIS.

Given the forecast for continued economic growth, but at a pace which comes up short of recent norms, look for some slowing in the rate of personal income expansion in the coming year in Pennsylvania. Also, in that the slowdown is likely to be concentrated in goods producing activities, the service producing side will have to carry the load. While the disparities between east and west remain, they are not quite as pronounced as in years past. Nonetheless, the west is unlikely to make up for much of the ground lost in previous years anytime soon.

— William D. Anderson

Building Permits Report

Building activity in Pennsylvania continues to ease from its record-setting pace of the mid 1980s. While trends are not especially encouraging relative to previous years, they should not be interpreted too negatively. The current slowdown simply represents a cyclical downturn. Recent trends certainly do not point to recessionary conditions in the Commonwealth's building-related industries.

Statewide, the Bureau of the Census reports that 15.5 percent fewer new houses in Pennsylvania have been authorized by permit in 1989 compared to the previous year. All told, 45,483 new housing units have been permitted in 1989. This represents the second straight drop in permit activity following five consecutive years of gains and it is the steepest annual decline since 1981 (chart). A good portion of the decline is concentrated in the single-family sector where nearly 17 percent fewer new units have been authorized. The decline on the multi-family side is less than one-half that amount (chart). This is the first time since 1982 that trends on the multi-family side are a bit more encouraging than for single-family projects.

New authorized construction in permit issuing places in PA (res. authorizations in units; nonres. authorizations in bldgs.; value in thousands of dollars)

	Authorizations		Value	
	1989	Pct. chg. from 1988	1989	Pct. chg. from 1988
Residential	45,483	−15.5	3,424,442	−11.4
Single-family	37,653	−16.9	3,097,316	−12.4
2 units	582	−26.1	24,974	−23.7
3-4 units	910	− 3.3	46,847	13.5
5+ units	6,338	− 6.9	255,305	1.3
Nonresidential	22,382	− 3.2	2,131,748	− 8.8
Amusement	201	− 1.0	37,116	−30.2
Religious	125	−13.2	48,940	31.2
Industrial	869	− 2.4	396,655	16.4
Parking garages	37	−24.5	36,384	−50.8
Service stations	268	− 5.0	31,588	16.0
Hospitals	88	−30.2	101,198	−38.0
Offices	788	− 1.3	583,485	−30.9
Public works	178	− 4.8	212,433	464.0
Schools	106	5.0	62,731	25.1
Stores	1,452	−12.3	447,825	−17.9
Other buildings	11,588	1.1	118,561	7.9
Non-building	6,682	− 7.6	54,832	0.5

Source: U.S. Dept. of Commerce, Bur. of the Census.

A reversal is also noted relative to nationwide trends. During the early 1980s, Pennsylvania's construction sector was hit much harder than the U.S.' by the back-to-back recessions. However, over the 1984-1988 period, the State turned in a relatively strong performance on the construction front. In 1989, however, Pennsylvania's decline in residential building activity is nearly twice as large as in the nation.

On the single-family side, permit values average $82,260 Statewide, up 5.3 percent from a year ago. This is less than one-half the gain averaged over the 1984-1988 period. The total value of all residential permits, at $3.4 billion, is off 11.4 percent from 1988.

Within the State, new housing units authorized by permit in 1989 are down in ten of the Commonwealth's 15 metropolitan areas. The largest gains are found in Beaver and Lycoming Counties, each with gains near 50 percent. The largest declines are found in the east. In the Allentown-Bethlehem region, authorizations are down by nearly one-third from 1988 readings. The five Pennsylvania counties in the Philadelphia metro area combine for 25 percent fewer permits. Authorizations in the Pittsburgh region are off nearly 16 percent. All told, growth eased in 11 of the 15 regions relative to 1988 (chart). In the group of 34 counties not included in a metro area, 22 have permitted fewer new houses than in 1988. Again, further slowing is evident in the northeast. Pike (−10.8 percent) and Wayne (−21.5 percent) Counties each authorized fewer new permits in 1989. After Pike's 1,499, Butler County permitted the largest number of new houses, 902, in 1989 for a minimal gain of just 2.7 percent.

Trends on the nonresidential side are also far from impres-

New authorized residential construction in permit issuing places by metropolitan statistical area and county (authorizations in units; value in dollars)

	Total				Single-family			
	Authorizations		Value		Authorizations		Value	
	1989	Pct. chg. from 1988	1989	Pct. chg. from 1988	1989	Pct. chg. from 1988	1989	Pct. chg. from 1988
MSAs								
A'town-Beth MSA	2,428	-31.9	205,973,701	-30.7	2,020	-38.2	191,299,546	-32.6
Carbon	256	-21.0	19,907,707	- 2.5	234	-16.1	19,477,707	5.3
Lehigh	1,141	-28.1	97,841,114	-30.1	955	-34.1	91,290,837	-31.4
Northampton	1,031	-37.6	88,224,880	-35.6	831	-46.1	80,531,002	-39.2
Altoona MSA (Blair)	343	3.0	19,651,926	- 7.4	274	1.9	18,024,926	6.7
Beaver MSA (Beaver)	431	48.1	32,292,438	55.4	366	30.2	29,722,813	44.9
Erie MSA (Erie)	931	20.1	50,431,325	20.6	546	-14.4	34,692,325	- 8.9
H'burg-Leb-Carl MSA	3,257	-10.3	222,497,543	- 2.8	2,773	- 6.1	202,835,882	- 0.1
Cumberland	1,362	- 7.5	94,259,497	- 5.5	1,049	-12.3	81,724,717	- 6.5
Dauphin	1,107	-22.7	83,731,970	- 6.8	1,080	-12.8	83,272,675	- 1.4
Lebanon	377	-21.5	21,488,380	-22.3	249	-21.7	15,983,794	-22.5
Perry	411	67.8	23,017,696	95.4	395	96.5	21,854,696	105.9
Johnstown MSA	466	- 9.5	26,897,191	- 9.4	412	-18.7	24,494,291	-16.7
Cambria	203	6.3	13,748,487	26.3	181	- 1.1	12,595,587	18.5
Somerset	263	-18.8	13,148,704	-30.0	231	-28.7	11,898,704	-36.7
Lanc MSA (Lancaster)	3,126	-11.2	239,129,793	- 7.0	2,385	-20.2	198,128,710	-15.6
Philadelphia MSA	11,432	-25.3	955,173,484	-22.3	9,093	-27.9	857,374,504	-22.8
Bucks	3,014	-29.7	230,151,943	-29.6	2,384	-36.8	208,997,026	-32.6
Chester	3,171	-16.0	321,425,330	-13.8	2,567	-28.3	295,672,329	-19.2
Delaware	1,101	-30.4	91,468,817	-27.4	794	-26.5	72,816,534	-24.8
Montgomery	3,546	- 9.0	265,927,320	-12.4	2,944	-14.7	242,568,030	-15.0
Philadelphia	600	-66.0	46,200,077	-53.7	404	-44.8	37,320,585	-28.7
Pittsburgh MSA	4,666	-15.9	414,883,898	2.1	3,794	- 1.2	383,401,475	7.6
Allegheny	2,859	-19.8	276,715,831	3.3	2,073	- 2.7	247,680,300	9.6
Fayette	278	-25.3	13,878,399	-10.2	263	4.4	13,482,899	12.1
Washington	552	4.7	41,421,594	- 0.1	513	8.9	40,761,594	2.6
Westmoreland	977	- 9.9	82,868,074	1.6	945	- 4.4	81,476,682	3.9
Reading MSA (Berks)	2,125	- 2.7	153,150,268	4.8	1,832	-10.5	140,459,190	- 0.8
Scr-Wilkes-Barre MSA	4,906	-11.2	350,530,130	- 5.1	4,248	-12.0	322,164,838	- 4.8
Columbia	114	-12.3	6,170,142	6.4	108	- 1.8	6,032,642	12.7
Lackawanna	785	9.9	57,634,620	29.8	692	5.8	54,874,994	27.5
Luzerne	1,323	13.4	85,631,227	21.3	1,056	4.9	74,129,455	21.3
Monroe	2,614	-24.2	197,429,605	-19.2	2,336	-22.0	183,873,211	-18.3
Wyoming	70	7.7	3,664,536	-11.4	56	- 5.1	3,254,536	-15.6
Sharon MSA (Mercer)	190	- 2.6	11,709,999	9.4	162	- 5.3	10,948,999	12.8
St Coll MSA (Centre)	824	17.2	59,370,912	2.8	496	-22.1	40,869,840	-22.9
W'port MSA (Lycoming)	532	47.0	26,025,304	29.3	267	-11.6	18,734,623	- 0.6
York MSA	3,033	-20.8	218,377,121	- 3.6	2,755	- 4.5	206,009,337	2.7
Adams	705	-23.0	47,471,434	-12.3	645	-13.4	45,083,591	- 6.4
York	2,328	-20.1	170,905,687	- 0.9	2,110	- 1.4	160,925,746	5.5
Non-MSA counties								
Armstrong	91	7.1	4,354,334	- 2.5	62	-27.1	3,516,134	-21.3
Bedford	129	- 5.1	6,001,787	4.1	129	7.5	6,001,787	15.8
Bradford	120	-10.4	7,120,844	18.8	108	- 6.1	7,038,270	21.0
Butler	902	2.7	80,044,983	6.8	756	5.9	73,626,069	7.6
Cameron	9	-30.8	623,456	-26.7	9	-30.8	623,456	-26.7
Clarion	52	-16.1	2,627,267	- 9.8	46	-25.8	2,537,267	-12.9
Clearfield	82	-13.7	5,324,262	2.1	74	-10.8	5,164,262	4.1
Clinton	80	-12.1	4,225,771	-13.8	57	- 9.5	2,918,271	-11.0
Crawford	173	- 1.7	7,474,009	6.2	161	- 6.9	6,724,009	- 2.7
Elk	87	- 4.4	4,599,363	5.0	77	- 3.8	4,385,363	5.4
Forest	14	27.3	471,621	-16.7	14	27.3	471,621	-16.7
Franklin	378	-37.3	25,240,987	-24.9	378	-37.3	25,240,987	-24.9
Fulton	39	0.0	2,305,656	36.1	39	0.0	2,305,656	36.1
Greene	8	-38.5	456,860	-33.5	8	-27.3	456,860	-30.8
Huntingdon	163	19.9	5,810,809	25.7	159	16.9	5,639,447	22.0
Indiana	79	-47.3	7,529,620	-18.4	65	-33.7	6,789,620	- 4.7
Jefferson	91	31.9	4,523,500	30.0	91	31.9	4,523,500	30.0
Juniata	78	- 9.3	3,198,525	3.0	66	- 5.7	2,942,525	6.9
Lawrence	258	89.7	11,137,402	56.7	136	19.3	7,969,902	18.5
McKean	60	9.1	3,219,373	27.2	60	15.4	3,219,373	29.5
Mifflin	129	-28.7	6,394,898	-21.1	125	-30.2	6,239,898	-22.4
Montour	204	-16.0	7,986,768	5.6	204	-16.0	7,986,768	5.6
Northumberland	237	8.2	10,777,043	11.7	195	22.6	9,654,143	23.1
Pike	1,499	-10.8	120,124,100	-30.2	1,417	-14.0	116,484,100	-31.7
Potter	43	87.0	1,200,715	59.7	43	87.0	1,200,715	59.7
Schuylkill	271	7.1	16,974,132	28.0	269	9.8	16,904,132	28.7
Snyder	73	-34.8	4,650,861	-22.2	73	-29.8	4,650,861	-19.8
Sullivan	70	-11.4	3,406,581	3.7	70	-11.4	3,406,581	3.7
Susquehanna	175	-15.5	8,466,762	-10.8	168	-13.8	8,357,762	- 9.8
Tioga	187	-20.1	7,936,915	- 3.8	185	-20.9	7,886,915	- 4.4
Union	145	-16.2	9,428,301	-16.5	139	- 5.4	9,176,801	- 1.3
Venango	49	-29.0	2,262,307	-32.9	49	-29.0	2,262,307	-32.9
Warren	97	38.6	3,858,260	15.7	79	12.9	3,300,500	- 1.0
Wayne	750	-21.5	50,734,712	-16.3	748	-21.6	50,694,712	-16.2

Source: U.S. Dept. of Commerce, Bur. of the Census

New authorized nonresidential construction in permit issuing places by metropolitan statistical area and county (authorizations in no. of bldgs.; value in dollars)

	Authorizations		Value	
	1989	Pct. chg. from 1988	1989	Pct. chg. from 1988
MSAs				
A'town-Beth MSA	1,859	-14.4	112,488,167	-30.0
Carbon	112	-21.7	4,430,144	3.2
Lehigh	823	- 7.7	57,618,787	-39.2
Northampton	924	-18.7	50,439,236	-18.2
Altoona MSA (Blair)	173	- 2.8	16,875,411	2.8
Beaver MSA (Beaver)	309	-17.2	9,520,775	-28.5
Erie MSA (Erie)	536	- 7.4	22,549,354	-40.4
H'burg-Leb-Carl MSA	1,502	- 2.0	224,269,582	2.1
Cumberland	498	-13.2	44,642,309	-46.6
Dauphin	658	9.8	136,733,098	50.2
Lebanon	217	0.9	40,884,050	- 5.7
Perry	129	-11.0	2,010,125	27.3
Johnstown MSA	357	2.0	196,572,283	1099.0
Cambria	186	26.5	183,401,329	1727.3
Somerset	171	-15.8	13,170,954	107.2
Lanc MSA (Lancaster)	1,446	- 2.1	113,109,332	3.1
Philadelphia MSA	4,950	-11.3	635,611,762	-38.3
Bucks	1,558	-25.9	112,206,076	-15.3
Chester	1,199	- 0.7	127,196,639	0.9
Delaware	558	-15.1	119,504,959	110.8
Montgomery	1,474	4.2	190,769,197	- 5.2
Philadelphia	161	-18.7	85,934,891	-83.3
Pittsburgh MSA	2,333	0.0	253,328,912	21.9
Allegheny	1,168	1.1	168,539,014	12.9
Fayette	239	-14.3	10,312,022	35.9
Washington	410	- 3.5	22,187,227	4.3
Westmoreland	516	8.9	52,290,649	75.6
Reading MSA (Berks)	717	29.0	52,506,519	-39.6
Scr-Wilkes-Barre MSA	1,236	7.3	114,922,595	15.6
Columbia	110	4.8	4,524,132	176.3
Lackawanna	273	16.2	25,064,147	- 3.4
Luzerne	455	11.0	63,597,260	45.6
Monroe	367	- 3.2	20,842,270	-24.8
Wyoming	31	34.8	894,786	115.3
Sharon MSA (Mercer)	292	5.8	16,419,963	57.4
St Coll MSA (Centre)	272	-20.0	37,102,142	3.3
W'port MSA (Lycoming)	330	19.1	20,735,896	96.0
York MSA	1,776	3.7	91,923,060	- 0.4
Adams	275	9.1	13,101,803	13.6
York	1,501	2.7	78,821,257	- 2.4
Non-MSA counties				
Armstrong	100	5.3	2,751,711	24.6
Bedford	135	- 0.7	3,628,064	-8.0
Bradford	260	-18.2	7,413,844	30.6
Butler	356	- 0.3	38,848,398	-21.4
Cameron	19	171.4	711,998	11.0
Clarion	69	40.8	951,423	2.8
Clearfield	55	12.2	3,884,189	8.0
Clinton	70	9.4	2,129,021	-25.9
Crawford	408	-23.3	13,642,992	59.1
Elk	162	- 1.2	6,031,989	156.1
Forest	6	-53.8	76,000	55.5
Franklin	217	38.2	18,365,926	323.6
Fulton	64	-32.6	1,731,264	281.2
Greene	7	-53.3	30,415	-93.7
Huntingdon	91	4.6	5,667,638	97.1
Indiana	48	-34.2	4,989,970	34.6
Jefferson	111	- 0.9	5,291,945	73.5
Juniata	62	31.9	2,130,714	105.0
Lawrence	129	-13.4	11,896,834	105.5
McKean	106	11.6	4,140,846	-27.8
Mifflin	108	10.2	3,024,286	-62.6
Montour	13	-40.9	1,327,250	-89.7
Northumberland	164	27.1	20,485,682	185.3
Pike	237	49.1	7,725,396	18.7
Potter	70	9.4	550,891	-39.2
Schuylkill	148	- 5.1	10,886,623	- 4.6
Snyder	133	- 0.7	3,993,473	-17.1
Sullivan	40	-24.5	650,030	72.2
Susquehanna	102	- 5.6	1,771,774	-30.6
Tioga	255	14.9	4,208,565	- 4.8
Union	92	-22.0	4,626,980	-66.6
Venango	64	-25.6	7,134,279	236.6
Warren	169	11.9	3,550,014	66.9
Wayne	235	88.0	11,162,834	106.5

Source: U.S. Dept. of Commerce, Bur. of the Census.

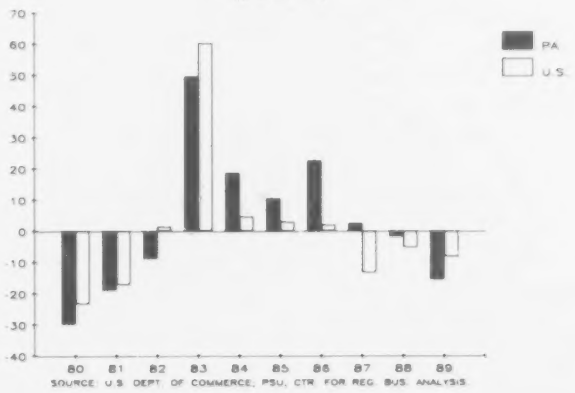
sive. Throughout the State, the number of new projects authorized by permit, 22,382, are off more than 3 percent for the year and are down 8.8 percent in terms of total valuation. The three largest building categories — stores, industrial buildings, and offices — are off 12.3, 2.4, and 1.3 percent, respectively.

In terms of geographic trends, permit authorizations are off in eight of the State's 15 metro areas. In the Philadelphia region, more than 11 percent fewer authorizations have been granted while the four-county Pittsburgh region finds authorization totals unchanged from a year ago. In the nonmetro portions of the Commonwealth, there are 16 counties recording increases over the year to go alongside 18 counties with declines in nonresidential permit authorizations.

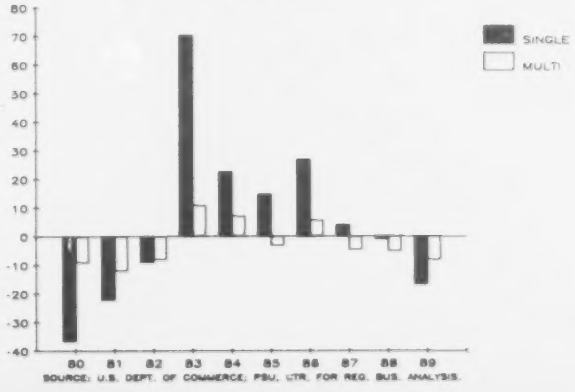
It is quite unlikely that growth in overall building activity similar to that recorded in the mid 1980s will be repeated any time soon. On the residential side, relatively high housing prices and the probable satisfaction of pent-up demand argue against any significant turnaround in the near-term. Over the long-run, demographic forces will likely limit potential gains in housing activity. Simply put, the population of potential homebuyers may be shrinking, at least in relative terms, in Pennsylvania.

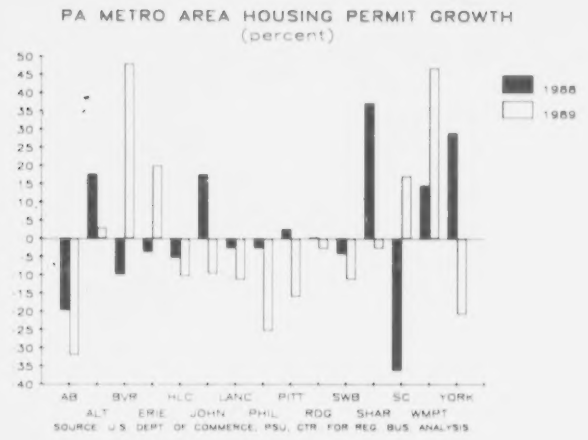
This is not to say that there will not be periodic cyclical improvement in the construction sector's fortunes in Pennsylvania, most likely in response to favorable credit conditions. Indeed, should the current downtrend in interest rates be a sign of things to come, some slight improvement later in 1990 may be apparent. However, the combination of low

PA AND U.S. HOUSING PERMIT GROWTH
(percent)



PA SINGLE- & MULTI-FAMILY HOUSING PERMIT GROWTH
(percent)





borrowing costs and fairly strong economic growth, similar to the situation which prevailed during the mid 1980s and contributed greatly to the strong showing on the part of construction, just is not in the cards. Until such a scenario unfolds, construction trends will likely remain unimpresive. Indeed, preliminary data for the first four months of 1990 show that permit activity in the State continues to fall at a rate similar to that for 1989, though some improvement over 1989 growth trends is noted in the Philadelphia and Pittsburgh regions.

— William D. Anderson

Focus on the U.S. Economy

Those involved in the publication of the Pennsylvania Business Survey *are constantly striving for consistency in reporting on economic conditions and trends as they relate to the Commonwealth. As a result, several dominant or overriding themes are often used as reference points and serve as common denominators in our analyses. Several times in the past, the ties between the Pennsylvania and U.S. economies have been highlighted. In order to keep readers updated on all factors having an impact on Statewide economic conditions, it is felt that it is worthwhile to provide a thorough overview of U.S. economic conditions on a periodic basis. This represents the third consecutive year that the June issue of the* Survey *focuses in on the national economy.*

Economists from five leading banks in Pennsylvania have agreed to provide commentary on U.S. economic conditions. The views expressed below are those of the contributors and do not necessarily reflect those of The Pennsylvania State University or the individual financial institutions. The Center for Regional Business Analysis gratefully acknowledges the contributions of each of the participants.

Jake Haulk, Vice President and Senior Economist, Mellon Bank, N.A., Pittsburgh, Pennsylvania.

While the underlying course of activity is still difficult to assess, most of the recent evidence points to a subpar growth rate over the balance of 1990. The prospects of a broad-based decline in construction activity, little if any growth in government spending and only scattered gains elsewhere in the economy argues in favor of growth in real GNP which may be less than 2 percent. Such a performance when coupled with inflation in the 4-5 percent range implies that the U.S. economy has moved into a stagflation-like environment.

The prospects for construction activity are bleak. An early or decisive reversal of the slump in housing starts seems unlikely in the face of firm interest rates and constraints on real estate lending imposed by increasingly stringent regulatory standards. Likewise, the plunge in contract awards for commercial and industrial construction points to declining expenditures over the balance of this year and possibly a good part of 1991 as well. As one convincing illustration, the trend of contract awards for office building construction has now fallen to its lowest level in at least ten years. In sum, the emerging picture is one of recession in the construction sector.

Strong gains in consumer spending are not in the cards for 1990. While real outlays for services, notably health care, are projected to climb at a spirited 3-4 percent annual rate, the outlook for spending on goods looks much less favorable. Briefly stated, the slowdown in job and income growth along with high debt burdens and some erosion of confidence is expected to dampen the demand for both durable and nondurable goods. The looming possibility of increased taxes at the federal, state and local levels must also be regarded as another potential negative in the outlook for many consumer markets. Against this backdrop, our latest forecast for real purchases of goods shows a feeble growth rate of 1 percent between the fourth quarter of 1989 and the final quarter of this year. We seriously doubt, therefore, that consumer spending can provide the impetus for a significant pickup in the rate of overall economic growth during 1990.

Despite the worrisome slump in contract awards for new manufacturing facilities, we are still forecasting moderate increases in spending for new equipment. Unfortunately, the risks to this forecast are mostly on the downside. During the post-World War II period, declines in corporate profits and cash flow have usually been followed by cutbacks in the growth of business investment outlays. Given last year's sharp decline in corporate profits, therefore, the best that might be expected for investment spending in 1990 is a year-over-year gain of between 3-4 percent. Nonetheless, an increase of this magnitude implies that business investment should continue to support a rising trend of overall economic activity over the balance of 1990.

In real terms, federal, state, and local government spending for goods and services is likely to be flat or even slightly downward during the remainder of 1990. Aside from the near certainty of cuts in defense spending, outlays in the public sector will be severely constrained by the mounting fiscal problems of state and local governments. On this point, it might be noted that at the end of last year the operating budget deficits of state and local governments — excluding social insurance funds — increased to a record yearly rate of almost $46 billion.

Notwithstanding the prospect of slow economic growth in the U.K. and Canada, U.S. exports in real terms should continue to climb at a healthy yearly rate of close to 7 percent through the balance of this year. But since imports are projected to increase at a near-6 percent rate, we are forecasting that the real net export balance will approximate $50 billion in 1990, representing a small improvement over last year's

$52.6 billion. In other words, the foreign trade sector will only make a minor contribution to this year's economic growth rate.

Unfortunately, there are formidable difficulties in the path of a sustained reduction in the inflation rate. Not only are prices in the service sector likely to rise at a rate above 5 percent, but industrial commodity prices could again trend upward in response to the buoyancy of economic conditions in most major countries. Bear in mind also that a firming of oil prices is to be expected if, as on similar occasions in the past, OPEC is ultimately able to curtail overproduction. Thus, notwithstanding April's low 0.2 percent increase in consumer prices, our latest forecast again shows an inflation rate of around 5 percent for the year as a whole.

Since we do not expect a quick change in Fed policy, our latest forecast looks for little material change in either short- or long-term interest rates over the next couple of months. Looking beyond the next 2-3 months, our expectation that the economy will remain in low gear suggests that there is room for a modest — 25-50 basis point — decline in interest rates.

Stuart G. Hoffman, Senior Vice President and Chief Economist, PNC Financial Corp., Pittsburgh, Pennsylvania

Real GNP rose by just 1.25 percent in the past two quarters — barely half of its long-run growth potential. Viewing the economy over these two consecutive quarters helps wash out the confluence of unusual events during this period. These included the Boeing strike and production rebound, the buildup and subsequent reduction in car production and inventories, and the mood swing of mother nature from frigid in December to hot flashes in January and February.

This spring brings the first opportunity to get a clearer read of economic conditions. As always, the evidence is mixed but leans heavily to the sluggish side. Payroll job growth ceased over the past three months, excluding the hiring of temporary census workers. Big job losses were widespread in the construction and manufacturing industries, which were about offset by new jobs in the service sector. Retail sales fell in March, April, and May. This is the first time retail sales fell for three consecutive months since early 1981. Auto sales were particularly weak last month and cars are again starting to pile up on dealers' lots. Auto production was up sharply in May and plans are to keep cars rolling off the assembly lines in the face of a possible strike next autumn. This improvement helped lift the Purchasing Managers' Index to 50.7 — its second straight reading above 50. Aggressive production plans, mixed with weak car sales, could spell trouble for auto makers, dealers, and suppliers. Construction spending fell in March and April with housing starts and sales reaching their lowest levels since the current expansion began in 1983. Moreover, construction contracts for future building are at their lowest levels in the past five years.

In summary, we doubt the economy can show sustained improvement in the face of the financial industry's troubles. Consequently, real GNP gains for the remainder of 1990 and 1991 will remain below-average (and the balance of risks is on the downside).

Fed policymakers are doing their best to stay out of the line of fire until the smoke clears on the underlying trends in jobs, output and inflation. Moreover, the Fed would prefer to sit quietly while the politicians debate the budget deficit debacle. The Fed's "hawks" are likely feeling more comfortable with the current stance of policy now that M2 growth has subsided to well within its target range and commodity prices have stabilized. The Federal funds rate appears locked at 8.25 percent during the next few months before slipping to 7.75-8 percent by early autumn. That would take the bank prime rate down to 9.5-9.75 percent. The Fed has the luxury to hold to a steady policy while the bond market takes over the role of interest rate disciplinarian. Bond yields rose in early spring in reaction to indications of higher inflation and then yields fell as inflation readings improved.

A combination of stringent regulatory oversight, problems in commercial real estate and general economic concerns have led banks to prudently tighten business credit conditions in selected troubled industries and regions. This is a dynamic process and there will be instances of businesses denied credit, but the situation does not yet qualify as a nationwide "credit crunch" that could tip the U.S. economy into a recession.

Carol A. Leisenring, Executive Vice President and Chief Economist, CoreStates Financial Corp., Philadelphia, Pennsylvania

Despite some wide swings in perceptions about the health of the economy, neither the outlook for 1990 nor our forecast has changed much in the past few months. Since January, perceptions about the economy have swung from fear that a recession was imminent to concern about rising inflation and the potential for Fed tightening. Although periods of slow economic growth are often subject to such wide-ranging interpretations, the monthly data in 1990 has been skewed by a number of unusual, one-time effects that have made it difficult to ascertain the underlying strength of the economy. Fortunately, the economy itself is not as volatile as perceptions by Wall Street and the media would have one believe. Even so, swings in opinion concerning the economy are likely to persist for several months, and should in turn lead to similar swings in expectations about interest rates and the course of Federal Reserve policy.

To be sure, the first quarter contained an inflation scare, but we believe the worst news on inflation for the year is now behind us. The consumer price index rose 8.5 percent in the first quarter, the largest quarterly increase since 1982. Underlying that rate were substantial increases in food (11 percent), energy (28 percent), and apparel (23 percent) prices. The increase in both food and energy costs were to a large extent caused by earlier, unfavorable weather patterns, the effects of which are already reversed; world oil prices have also dropped by 20 percent since January. The increase in apparel prices is more mystifying, but it is possible that seasonal patterns are responsible for much of the increase. Thus, the items that boosted first quarter inflation will at least be better-behaved in the coming months.

So the inflation rate is not going to remain at 8.5 percent as was the concern in the financial markets in April. We have raised slightly our inflation forecast for the year, but at 4.5 percent it remains in the range of experience over the past several years. The disappointing aspect of the inflation outlook is that there seems little likelihood of its improving below the 4.5 percent range. While the factors that have exacerbated inflation in the first quarter are already subsiding, some elements of the inflation rate, such as medical care and housing, show no sign of moderation.

While the financial markets will apparently be happy to see inflation return to what has become its "usual" pace, the Federal Reserve has repeatedly indicated that 4.5 percent inflation is not an acceptable long-run result. Given the Fed's desire to ratchet down the inflation rate, the first quarter bulge in the price level, and the associated rise in long-term interest rates that occurred in late April-early May, the case for Fed easing at this point is hardly overwhelming, regardless of how weak or strong the economy is. The Fed will need to see more favorable inflation patterns and additional evidence of economic weakness before an easier monetary policy could appear warranted. The better inflation numbers released in recent weeks are helpful in that regard, but the Fed is likely to want more than one month of data to be convinced. While there is evidence of a weaker economy, it is neither substantially weaker than expected, nor so weak that the Fed would be compelled to forestall a recession.

The bottom line is that while we still expect to see some additional interest rate declines, it may be mid-summer before they occur. There has been a small decline in short-term interest rates (20-40 basis points) in recent weeks, but any substantial and lasting decline in short rates (including a drop in the prime rate) is unlikely until the Fed eases. As long as the economy continues to expand, albeit modestly, a wait-and-see attitude by the Fed accomplishes more toward their inflation goal.

Bernard M. Markstein, Senior Economist and Vice President; Mark S. Uhle, Research Assistant, Meridian Bank, Reading, Pennsylvania

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The outlook is for slow growth in the U.S. economy. The forecast for real GNP growth in 1990 is 1.6 percent, with some pick-up in 1991. Automobile sales will average a lethargic 9.9 million units in 1990. Real estate and construction will also be in the doldrums. Housing starts will face another down year, averaging 1.37 million units for the year. The outlook for office construction is not any better. Robust office construction in the mid 1980s left a glut of unoccupied space. Thus, high vacancy rates and an increasingly cautious business sector are acting as a brake on this sector.

The latest economic numbers support our forecast. Payroll employment rose 164,000 in May, including 147,000 part-time census workers. In addition, April's figure was revised downward to a decline of 23,000. This represents the first decline in payroll jobs since June 1986. The weakness which was concentrated in the manufacturing sector now is creeping into the service sector as well. Looking at the second quarter, real GNP growth will be less than 2 percent at an annual rate, despite some restocking of inventories. The sluggishness in the economy will become more apparent in the labor markets, with the U.S. unemployment rate edging up to 5.6 percent by year's end.

Inflation, which averaged over 8 percent (as measured by the Consumer Price Index) in the first quarter of 1990, will moderate considerably. The Producer Price Index, often a harbinger of consumer inflation, has had two consecutive negative readings (March and April). April's CPI was also encouraging as both overall and core (non-food and energy) inflation rose only a scant 0.2 percent. We forecast the CPI to increase 4.6 percent in 1990.

The trade picture has darkened recently, but will improve gradually in the second half of 1990. March's merchandise trade deficit widened to $8.4 billion from $6.1 billion in February. This poor showing masked the fact that exports rose 4.6 percent to a record $33.3 billion. Unfortunately, imports grew 10 percent during March, as the lagged effects of 1989's strong dollar continued to be felt. Thus far in 1990, the dollar has exhibited some weakness against most currencies (the Japanese yen and West German Deutsche mark are notable exceptions). This should result in an improving trade picture later on in 1990 and into 1991. Over the longer-run, exports will be boosted by the opening of Eastern Europe.

Business fixed investment is forecast to slow in 1990. In the current economic environment, businesses are being more cautious. Most companies are re-examining their capital spending plans. Meanwhile, facing the same uncertain environment, banks are scrutinizing loan applications more carefully. Thus, with both businesses and banks leery of a recession, business fixed investment will increase only 2.6 percent in 1990.

In summary, the baseline forecast is for slow growth in 1990, with no recession and no negative quarters. By 1991, the U.S. economy will begin to pick up strength again.

Joel L. Naroff, Senior Economist, First Fidelity Bancorporation, Philadelphia, Pennsylvania

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The economy is in a period of slow economic growth and tight monetary policy that implies both declining inflation and interest rates as we go through the second half of 1990. This can and should occur without a recession.

In early 1990, temporary factors drove inflation and interest rates higher. Jumps in energy and food prices due to abnormally cold weather created an impression of rising inflation. Indeed, the 7.1 percent increase in the Consumer Price Index (CPI) in the first quarter 1990 was the highest since second quarter 1982. However, as the cause of the rising CPI was a one-time event, the inflation rate subsequently dropped dramatically, to an expected 3.5 percent second quarter rate, while producer prices have been essentially flat for the past four months.

In contrast to the temporary weather-driven price changes, the underlying inflation rate, which fundamentally determines the trend in price increases, is affected by the relationship between demand (GNP) growth and productive capacity (supply). Here, the conditions all point to declining inflation, as household consumption is slowing, businesses are easing investment activity in the face of the slackening demand, and monetary policy remains tight.

In the second half of 1990, real consumption is expected

to grow by only 1.5 percent, compared to an average of 3 percent over the past three years. Personal income growth has slowed, consumer confidence is waning, and as a result, the willingness of households to take on additional debt has receded. Businesses, in the face of weak demand and mediocre corporate profits, have recently cut back on their investment plans. Finally, a federal budget deficit reduction compromise will almost assuredly raise taxes and slow spending growth, making fiscal policy less expansive. Indeed, the only area of expanding demand appears to be in the export sector. Thus, the spending patterns of households, businesses, and the government sector all point to slower real growth.

Part of this slowing in the economy can be traced to the tight monetary policy on the part of the Federal Reserve. Money supply growth has come to a standstill. Since monetary policy affects the economy and inflation with a lag, the springtime tightening will be felt in the second half of the year.

The impact of the double-barrelled real economic and monetary slowdown can already be seen. In the second quarter, employment growth in the private sector will be flat at best, and may even decline. Although manufacturing employment has been falling for a year, there is weakness now in the service producing sector. This is a positive sign for inflation. In the manufacturing sector, capital investment and more productive labor has led to rising productivity and lower unit labor costs. This has reduced operating costs and made manufacturing firms more competitive. The same process has to occur in the services sector, and the slower employment expansion may be a sign that it is finally beginning. If that move to controlling cost and raising productivity has started, the increase in service sector unit labor costs, which were in excess of 7 percent during the first quarter, should moderate, further reducing pressures on prices.

Finally, the sharp rises in worldwide interest rates, especially in Germany and Japan, that helped drive U.S. rates up in the winter and early spring have ended. Stability in the Japanese stock market has generated more stable interest rates in Japan. The German situation, however, is the one clear negative for our rate decline forecast. German currency and economic reunification could create greater upward pressure on German rates. However, this will be due, at least in part, to rising inflationary expectations, and will not necessarily cause U.S. rates to rise.

All of these signs point toward an easing of inflation and should lead to a moderate decline in interest rates over the next six months. Longer-term rates should decline first, with the short-end waiting to see when the Fed may be ready to ease. The Fed will not act until it is certain that inflation has decelerated, which would be indicated by additional low consumer and producer price increases as well as a real budget deficit reduction agreement. We expect that the prime rate could decline twice, to 9.25 percent from the present 10 percent level, mortgage rates should fall another 50 basis points to below 10 percent, the federal funds rate could decrease to 7.75 percent, and long-term treasury bonds may fall to 8 percent or even lower. Interest rates are coming down.

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